SUPREME COURT, U. S.

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IN THE

Supreme Court of the United States

October Term, 1968

No. 341

ESTATE OF EUGENE L. FREELAND, Deceased, by SECURITY FIRST NATIONAL BANK, a national banking association, Executor, and VERA GOOD FREELAND, by L. N. TURRENTINE, Conservator,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

MARGARET C. LOWTHIAN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

GEORGE T. ALTMAN,
424 South Beverly Drive,
Beverly Hills, Calif. 90212,

ADAM Y. BENNION,
523 West Sixth Street,
Los Angeles, Calif. 90014,

Attorneys for Petitioners.

Parker & Son, Inc., Law Printers, Los Angeles. Phone MA. 6-9171.

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ESTATE OF EUGENE L. FREELAND, Deceased, by SECURITY FIRST NATIONAL BANK, a national banking association, Executor, and VERA GOOD FREELAND, by L. N. TURRENTINE, Conservator,

Petitioners,

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MARGARET C. LOWTHIAN,

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Respondent.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

Petitioners hereby petition this Court for a writ of certiorari to the United States Court of Appeals for the Ninth Circuit. These two cases were consolidated in the courts below and are joined here in this petition.

Opinions Below.

The memorandum findings of fact and opinion of the Tax Court are unofficially reported by CCH at 25 TCM 1473. An original opinion of the Court of

Appeals, rendered March 8, 1968 [R1; App. 1][1], was modified by an "Order on Petition for Rehearing", issued May 6. 1968 [R1; App. 30]. As so modified the opinion is reported at 393 F. 2d 573.

Jurisdiction.

The original decision of the Court of Appeals was entered on March 8, 1968 [R1; App. 1]. A petition for rehearing was filed on April 8, 1968 [R1]. On May 6, 1968, the Court of Appeals entered an "Order on Petition for Rehearing" denying the petition for rehearing but making certain changes in its opinion. [R1; App. 30]. On May 10, 1968, petitioners filed there a "Motion for Reconsideration of the Petition for Rehearing" [R1]. The Court of Appeals denied that motion on May 23, 1968 [R1]. The jurisdiction of this Court is based on 28 U.S.C. §1254(1).

Questions Presented.

We state here first certain of the facts in order to simplify the questions presented. This is a federal income tax case, involving generally the problem of capital gain versus ordinary income on the sale by the decedent, Eugene L. Freeland, hereinafter referred to as "Freeland," and by his secretary and business associate, Margaret C. Lowthian, hereinafter referred to as "Lowthian", of their respective partnership interests in a landholding partnership, Sam Berger Investment Company, hereinafter referred to, as by the courts below, as "SBIC." As the opinion below shows:

(1) There were two general partners, Freeland and one Sam Berger, hereinafter referred to as "Berger";

---

[1]The reference is to the volume of the Record, and to the page of the Appendix, *infra*.

and there were in addition certain limited partners, including Lowthian;

(2) The general business policy of SBIC was required by the partnership agreement to be determined by the mutual consent of the two general partners;

(3) The land acquired by SBIC consisted of 4500 acres, unsubdivided, but as part of the procedure of acquisition an option to purchase 500 acres, out of a designated 800-acre parcel of the land, was given by SBIC to a corporation organized for the purpose, Lake Murray Development Company, hereinafter referred to, as by the courts below, as "LMDC";

(4) Berger directed LMDC, and he, but not Freeland or Lowthian, had a capital interest in that corporation;

(5) LMDC exercised its option to the extent of 150 acres, and engaged in subdivision thereof and construction of homes;

(6) LMDC failed; it became insolvent May 4, 1956. Berger, because of that failure and his own sequential financial difficulties, entered, on August 10, 1956, into an agreement of sale of his partnership interest in SBIC to a nonmember, a group of developers hereinafter referred to as the "Tavares group," despite a provision in the partnership agreement against sale of a partnership interest to a nonmember;

(7) SBIC at no time engaged in any activities to develop or solicit for any of its land, except for said option relation with LMDC, which the courts below referred to as an "interlocking" relation;

(8) After the said date of Berger's sale of his interest, August 10, 1956, SBIC, or rather what was left

of it, was not involved in any manner, not even in that "interlocking" sense, in any plan or any activity to develop, or sell, or offer for sale any of its land;

(9) Berger did not get Freeland's consent to his sale of his interest, and Freeland, approached by the Tavares group after Berger's sale to them, refused to join them in development of the property because that would have meant competition by him with his own clients as civil and structural engineer;

(10) Freeland at first also refused to sell his interest to the Tavares group, but finally, on November 26, 1956, he, and also Lowthian, executed agreements to sell their interests to them.

It is the classification for tax purposes of the gain on those sales which is here involved. If SBIC was then holding its property primarily for sale to customers in the ordinary course of its trade or business, that gain of petitioners was ordinary income; otherwise it was capital gain. In this connection, petitioners contend, and on the basis of the facts stated above, that even if prior to the sale by Berger of his partnership interest, that is, August 10, 1956, SBIC was holding its property primarily for sale to customers in the ordinary course of its trade or business,—which petitioners do not concede, —after that sale by Berger, and because of it and prior events, SBIC's purpose had changed and it was not holding its property primarily for sale to customers in the ordinary course of its trade or business. The questions presented are as follows:

(1) On the basis of the facts stated above, was it not error of law for the Tax Court to conclude, in respect to the period after Berger's sale of his partner-

ship interest, August 10, 1956, that the land was being held by SBIC primarily for sale to customers in the ordinary course of its trade or business?

(2) If, as stated by the court below, as to the original purpose of SBIC regarding the land, the Tax Court "might possibly have properly found in petitioners' favor," had not petitioners, on the question of the said original purpose, carried their burden of proof?

(3) If, as stated by the court below in its original opinion, the petitioners' contentions of change of purpose were "admittedly not without support," and there would "perhaps have been considerable basis for a finding" in accordance with them, had not petitioners, on the question of change of purpose, carried their burden of proof?

(4) In respect to question (3) above, is the answer different if the opinion of the court below is taken instead as modified by its "Order on Petition for Rehearing," with, therefore, the word "wholly" inserted before the words "without support," and the word "some" substituted for the word "considerable"?

(5) Was not the burden of proof in any event on respondent because the case, having once been closed in the Treasury Department, was reopened there, not because the prior decision for petitioners was incorrect, but only because of the amount involved and in order to be consistent with the treatment by another agent of other partners of SBIC?

Statutes Involved.

The statutes involved are set forth in the opinion of the Court of Appeals, and as there set forth appear in the Appendix, *infra*, at pp. 3-4 thereof.

Statement.

The basic elements of fact involved are stated above by way of introduction to the questions presented. We add here certain facts which may be helpful. Berger's interest in SBIC was 20% as general partner, and 20% more as trustee of limited partnership interests of his two sons. Freeland had a 32% interest as general partner, and Lowthian had an 8% interest as limited partner. The remaining 20% was held as a single limited interest by another group, the owners with Berger of LMDC. That group acquired that 20% interest, and the 500-acre option above referred to, as compensation for providing a deposit for off-site improvements required by SBIC's vendor. Lowthian sold her interest to the Tavares group at the same time Freeland did, and the latter 20% group sold theirs to the same vendees on October 31, 1957.

A fair statement of the remaining background of this case is contained in the quotations by the court below from the findings of the Tax Court. However, two paragraphs of the Tax Court's findings, giving the genesis of the case in the Treasury Department, were omitted by the court below and are included herein separately, in the Appendix, *infra,* at page 29.

As it appears there, this case was originally closed in the Treasury Department on the basis of allowance of the claims of Freeland and Lowthian in their respective returns that their gain on the sale of their partnership interests was capital gain. Subsequently the cases were reopened there because of the amount involved and "in the interest of being consistent" with the determination made by another agent involving other members of SBIC. Those other members were the 20% group of

limited partners above referred to. The agent in their cases determined that the gain by them on the sale of their interests in SBIC was ordinary income and not capital gain. Instead of going to the Tax Court as Freeland and Lowthian did, however, they paid the additional taxes, filed claims for refund, and went into the United States Court of Claims. That Court, on June 14, 1968, after a careful study of the opinion herein below, finally decided nevertheless in their favor.[2] As a result, the consistency which the Treasury Department demanded by reopening the case of the petitioners herein was lost in a reverse conflict between the court below and the United States Court of Claims. It is in this context that we come before this Court.

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[2]There were two cases in the Court of Claims, *Morse v. United States,* reported at 371 F. 2d 474 (January 20, 1967), and *Ginsburg v. United States* and *Balton v. United States,* consolidated, ... F. 2d ..... (June 14, 1968). Just before the decision in *Morse* was rendered, on December 30, 1966, the decision of the Tax Court herein was filed, and on the basis of that decision the government, on February 20, 1967, filed a motion for reconsideration in *Morse*. At the same time that the Court of Claims rendered its decision in *Ginsburg* and *Balton*, June 14, 1968, it denied the government's motion for reconsideration in *Morse*.

REASONS FOR GRANTING THE WRIT.

1. The Decision Below Is in Clear Conflict With the Decisions of the United States Court of Claims in Morse v. U.S., 371 F. 2d 474 (January 20, 1967), and the Consolidated Cases of Ginsburg v. U.S. and Balton v. U.S., ... F. 2d ..... (June 14, 1968).

In *Morse* the Court of Claims, in respect to the sale by another partner of SBIC of his partnership interest, reached a conclusion the exact opposite of the opinion below. In *Ginsburg* and *Balton,* involving still other partners, the Court of Claims followed its conclusion in *Morse.* While the sales of partnership interests involved here took place November 26, 1956, and the sales involved there all took place October 31, 1957, almost a year later, those cases base their conclusion as to change of purpose on precisely the same events as those on which petitioners relied here. Those events were events terminating with the sale by Berger on August 10, 1956, events thus distinct from, and terminating well before, the sales involved here. See the opinion herein of the court below, Appendix, *infra,* at page 25 and that of the Court of Claims in *Ginsburg* and *Balton,* slip opinion, pages 4-5, 7.

Stating this very clearly the Court of Claims there says, at pages 4-5, in reference to its previous opinion in *Morse:* "It was our view that, no matter what the business of the partnership prior to the August date, the preponderance of the evidence indicated that all the problems and circumstances leading up to, and in-

cluding, Berger's contract of sale induced the partnership to give up its plans for developing the land and instead to continue to hold it but as investment property." Even more clearly showing that that court found the change of purpose to have already taken place at the time of Freeland's sale, footnote 14 on page 10 of the slip opinion in *Ginsburg* and *Balton* reads as follows: "We add that, in any event, we tend to the view, though we need not decide definitively, that the defendant has not given us a convincing reason for concluding that the property was held by the partnership as inventory on November 26, 1956, when Freeland and Lowthian sold their shares."

As the opinion there also shows, slip opinion, page 5, the government itself contended there that there was a conflict between *Morse* and the opinion herein below. The government there further contended, as shown at page 8 of the slip opinion, that on August 10, 1956, SBIC had abandoned its "primary purpose." Indeed, the Tax Court herein, as quoted by the court below, seems itself to have recognized this, although subconsciously, when it said, in reference to SBIC's indirect connection with development through LMDC, "the period of gestation was prematurely cut short". (App. 21). There is nothing in that to suggest that it would be attempted again.

The view of the Court of Claims regarding the conflict of opinions above shown, between itself and the courts herein below, is summarized on page 6 of its slip opinion in *Ginsburg* and *Balton*, as follows: "In fulfilling our judicial obligation, we have merely evaluated the facts differently than the Tax Court did in pursuit of its responsibility."

2. The Application by the Court Below of the Taxpayer's Burden of Proof Is in Clear Conflict With Decisions of Other Courts of Appeals and Decisions of This Court.

As to SBIC's original purpose, the court below states that the Tax Court "might possibly have properly found in petitioners' favor". (App. 24). As to petitioners' contentions of change of purpose, the court below there says, in its original opinion, they "are admittedly not without support," and there would "perhaps have been considerable basis for a finding" in accordance with them. As that court modified its opinion by way of its Order on Petition for Rehearing, it inserted the word "wholly" before the words "without support," and substituted the word "some" for the word "considerable." The court did not disclose on what evidence, or lack of evidence, those changes were based, nor did it disclose what those changes were intended to accomplish. But it is clear that the court thereby added to its uncertainty of language an attempt to inject precision of measurement into facts which could be the subject of broad evaluation but not precise measurement. In any case, those changes emphasize the difficulty of the court below in supporting the Tax Court's conclusion that petitioners were wrong, while acknowledging at the same time that the evidence showed they could be right.

The court below allowed the Tax Court's conclusion to stand because the burden of proof was on petitioner. (App. 23). The proof required to support petitioners being of a negative, that the property was not held pri-

marily for sale to customers in the ordinary course of trade or business, the burden of proof is less than if the proof required were of a positive. *Weir v. Commissioner* (C.A. 6) 283 F. 2d 675, 679. But even where the proof required is of a positive, what is required is only the preponderance of the evidence, therefore evidence showing that the facts asserted are more probably true than false. *Burch v. Reading Co.* (C.A. 3), 240 F. 2d 574, 579, cert. denied 353 U.S. 965. This Court has stated that requirement as the evidence which "would reasonably support a verdict for a plaintiff in an ordinary action for the recovery of money." *Burnett v. Niagara Falls Brewing Co.,* 282 U.S. 648, 654, 51 S. Ct. 262, 265; 2 Casey's Federal Tax Practice §8.7 at fn. 45, 9 Mertens §50.62 at fn. 23. We submit therefore that what the court below has in fact said here, in effect, is that petitioners have carried their burden of proof.

The burden of proof rule, moreover, may not be applied to defeat justice. *Helvering v. Taylor,* 293 U.S. 407, 55 S. Ct. 287, 9 Mertens §50.62 at fn. 22, §50.65 at fn. 60. Clearly, the statements of the court below, quoted above, show that the evidence was adequate to support petitioners, so that a decision against them would be inconsistent with justice.

3. The Opinion of the Court Below Is in Conflict With Decisions of This Court by Accepting Factual Inferences Made by the Tax Court on the Basis of Mere Suspicion.

This Court in *Commissioner v. Duberstein*, 363 U.S. 278, 292, 80 S.Ct. 1190, 1200, stated that factual inferences if not "mere suspicion" but factual conclusions based on "informed experience with human affairs" would come within the protection of the "clearly erroneous" rule. The inferences here, however, are framed in the very language of suspicion. Nor do they indicate a basis of informed experience.

For example, the 4500 acres acquired by SBIC, a mere seven square miles, "contained a lake, some canyons, and a mountain rising about 1100 feet above the surrounding terrain." (App. 6). Also, as to the mountain, the cost of offsite improvements was found to be prohibitive even at the foothills. (App. 18). Simple arithmetic would show that even with an average slope as high as 25%,[3] the mountain alone, with a floor radius then of 4400 feet, would rule out as unusable one-third of the 4500 acres. Yet the court below accepts the Tax Court's use of SBIC's average cost per acre based on the entire 4500 acres, including the mountain, in order to treat its selling price to LMDC for the non-mountainous portions of the land as a scheme for despoling the federal revenue. (App. 24).

We give the above only as one example of the character of the inferences made. Most of the others cited by the opinion below are of like character. (App. 23-

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[3]The maximum grade provided in San Diego is 15%, Council Resolution No. 173217.

24). We submit that those inferences, just as their very wording shows, do not rise above the level of mere suspicion.

4. The Opinion Below Is in Clear Conflict With Decisions of This Court in Failing to Apply the Language of the Statute as It Reads.

In *Malat v. Riddell,* 383 U.S. 569, at pp. 571-72, this Court held, in interpreting the word "primarily", as used in Section 1221(1) of the Internal Revenue Code, that that section should be applied as it reads. That section, being the one involved here, excludes from treatment as capital gain the gain on a sale of property held primarily for sale to customers in the ordinary course of trade or business.

The burden of the taxpayer, therefore, in order to show that that exclusion did not apply, would be to show, as observed above under Reason 2, that the property was not held primarily for sale to customers in the ordinary course of trade or business. As the court below concedes, the relevant intent is that held during the period immediately prior to sale. (App. 24-25). The findings as quoted by the court below show beyond any question that during the period immediately prior to the sales involved here, that is, prior to November 26, 1956, both LMDC and Berger then being out, the property was not held either primarily or at all for sale to customers in the ordinary course of trade or business. The court below makes no attempt to contest or in any manner to question this fact. What it does by way of answer is merely to say that during that period the partnership purpose regarding the land was "to some degree not clearly defined." (App. 25-26). If

the purpose was to some degree not clearly defined, just how it could be a purpose *primarily* held, the court below does not explain.

5. The Opinion Below Is in Clear Conflict With Decisions of This Court in Arriving at Its Conclusion by Way of an Obvious Non Sequitur.

This Court in *Tot v. United States,* 319 U.S. 463, 467, held that in arriving from "the fact proved" to "the ultimate fact presumed" reason as found in common experience was necessary. The opinion below in stating the petitioners' contentions on the question of change of purpose says: "They point, first, to the disputes that occurred between SBIC and LMDC; second, to the failure of LMDC; and third, to the sale of Berger's interest in SBIC to Tavares." (App. 25). Then, in the very next paragraph (as restated in its Order on Petition for Rehearing), it says, referring to the Congressional purpose of preventing partners from reducing their tax liability by converting potential ordinary income of the partnership into capital gain by selling their partnership interests: "This purpose would in many instances be frustrated if partners' decisions to sell their interests necessarily sufficed to establish the sort of 'change of purpose' which petitioners contend occurred here."

The implication in the sentence last quoted is that the petitioners were trying to establish a change of purpose of the partnership regarding the land on the basis of Freeland's decision to sell his interest, and Lowthian,

hers, and to apply the change of purpose so established to the determination of the character of the income involved in those very sales. This would, very plainly, be an attempt by the taxpayers to pull themselves up by their own bootstraps. Of course, the Congressional purpose indicated would be frustrated if such an attempt were allowed. But the court below points to no contention made by petitioners, at any point, in any document, attempting to rely for change of purpose upon their decisions to sell their own partnership interests. Thus the court below goes from the actual contentions of petitioners to an assumption of a contention which has no rational connection with them at all. This error is so self-evident that it should not be necessary to refer to any court decision to show it. We refer to the case of *Tot, supra,* nevertheless, in order to show that this Court has had occasion to recognize it.

What the court below may have meant, possibly, by the non sequitur shown above, was that it would not recognize a change of purpose at all, that the controlling purpose was the original purpose and not the purpose immediately prior to the sale involved. If that is true, then of course there is a clear and direct conflict with the United States Court of Claims, as the court below itself shows. (App. 24-25).

6. This Case Is Important Because of the Lack of Consistency Which Would Otherwise Remain in the Treatment by the Government of the Same Identical Facts in Respect to Different Taxpayers.

As observed under "Statement" above, the case here had originally been closed in the Treasury Department in favor of petitioners. It got into court because the Treasury Department reopened the case administratively in order to be consistent with the treatment of the same facts in the case of other partners of SBIC. If consistency was that important to the Treasury Department in its internal functioning, it certainly must be all the more important on the face of reported decisions. We believe that unless this conflict, described under Reason 1 above, is resolved, the harm to the Treasury Department, as well as to equality of justice to taxpayers generally, will be tremendous.

Conclusion.

We submit in conclusion for the reasons given above that this petition for a writ of certiorari should be granted.

Respectfully submitted,

GEORGE T. ALTMAN,
Attorney for Estate of Eugene L. Freeland, deceased, and Vera Good Freeland.

ADAM Y. BENNION,
Attorney for Margaret C. Lowthian.

Both by GEORGE T. ALTMAN,
Attorney.

APPENDIX.

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Opinion of the Court Below.

United States Court of Appeals for the Ninth Circuit.

Estate of Eugene L. Freeland, Deceased, by Security First National Bank, a national banking association, Executor, and Vera Good Freeland, by L. N. Turrentine, Conservator, Petitioners, vs. Commissioner of Internal Revenue, Respondent. No. 21,795.

Margaret C. Lowthian, Petitioner, vs. Commissioner of Internal Revenue, Respondent. No. 21,795-A.

[March 8, 1968]

On Petitions for Review of the Decisions of the Tax Court of the United States

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Before: BARNES, JERTBERG and ELY, Circuit Judges

BARNES, Circuit Judge:

On December 30, 1966, the Tax Court of the United States held in two related decisions that deficiencies existed in the Federal income tax of Eugene L. Freeland and Vera G. Freeland, husband and wife, for the years 1956-1961, and in that of Margaret C. Lowthian for the years 1956-1960. Eugene L. Freeland is now deceased, and his estate, along with Vera G. Freeland, now petitions this court under 26 U.S.C. § 7482 (1964), seeking review of the Tax Court's decision relating to them. Margaret C. Lowthian also petitions under the same statute for review of the decision in her case, and the two petitions have been consolidated for argument and decision.

In November 1956 the Freelands and Miss Lowthian (hereinafter refered to as "petitioners") sold their respective interests in a partnership, the Sam Berger Investment Company, the assets of which included approximately 4000 acres of land in San Diego, California. They reported the resulting gain on the installment basis as long-term capital gain, a tax treatment which was at first accepted by the District Director of Internal Revenue. In 1962, however, the District Director approved reopening with respect to 1956 (subsequent years are here involved because of utilization of the installment basis). On July 29, 1964, the Comissioner of Internal Revenue issued statutory de-

ficiency notices, asserting that the income from the sale of petitioners' partnership interests was ordinary income.[1] This position was sustained by the Tax Court, and the correctness of that ruling represents the major issue now before us.

The general statutory rule governing sales of partnership interests is stated in section 471 of the Internal Revenue Code, 26 U.S.C. § 741 (1964):

> "In the case of a sale or exchange of an interest in a partnership, gain or loss shall be recognized to the transferor partner. Such gain or loss shall be considered as gain or loss from the sale or exchange of a capital asset, except as otherwise provided in section 751 [26 U.S.C. § 751, *as amended* (Supp. II 1967)] (relating to unrealized receivables and inventory items which have appreciated substantially in value)."

The exception referred to, which is the basis for the Tax Court's decision, reads as follows:

> "§ 751. Unrealized receivables and inventory items.
>
> "(a) Sale or exchange of interest in partnership.
>
> "The amount of any money, or the fair market value of any property, received by a transferor partner in exchange for all or a part of his interest in the partnership attributable to—
>
> "...
>
> "(2) inventory items of the partnership which have appreciated substantially in value,

[1]The relevant period of limitations had been extended beyond the date of the notices by appropriate consents executed by petitioners.

shall be considered as an amount realized from the sale or exchange of property other than a capital asset.

". . .

"(d) Inventory items which have appreciated substantially in value.

". . .

"(2) Inventory items.

"For purposes of this subchapter the term 'inventory items' means—

"(A) property of the partnership of the kind described in section 1221(1) [26 U.S.C. § 1221(1) (1964)]. . . ."

The property described in section 1221(1) includes:

"stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayere primarily for sale to customers in the ordinary course of his trade or business. . . ."

Thus the basic issue here is whether the land owned by the petitioners' partnership was "held . . . primarily for sale to customers in the ordinary course of [its] trade or business." The Tax Court found that it was, and it is this finding which petitioners dispute.

The question thus posed is established by prior decisions as one of fact. *E.g., Richards v. Commissioner,* 81 F. 2d 369, 370 (9th Cir. 1936). Its determination depends upon a fairly complex series of events—a con-

There is no real challenge to those findings insofar as they relate to this background, and we therefore adopt them as our statement of facts:

> "Petitioners reside in San Diego County, California, and they filed their respective tax returns for the years in question with the district director of internal revenue at Los Angeles, California.
>
> "At all times material Lowthian was [Eugene L.] Freeland's secretary and business associate. Her participation in the transactions involved herein was through and with Freeland. . . .
>
> "From 1923 through the time of trial, Freeland has been a full time civil and structural engineer living and working in San Diego County, California. He is licensed to practice by California and certain other states and has been and continues to be a member of numerous professional engineering associations and societies. During the years involved herein, he was a senior member of a civil engineering firm and a structural engineering firm.
>
> "Freeland's practice has included land surveying, the design of municipal improvements, the subdivision of land, and the design of buildings and structures. He rendered professional services in some of the larger real estate developments in the San Diego area and included among his clients some of the area's most active real estate subdividers and developers. Because of the rapid growth of San Diego County prior to and during the years in question, and because of his excellent reputation, Freeland's practice has been financially successful. The growth of San Diego County has

also resulted in a continuing and substantial appreciation in real estate values.

"Among the many land developers employing Freeland and/or his civil engineering firm (hereafter referred to as the 'engineering partnership') were George T. Forbes and Theodore M. Jacobs, doing business as Kensington Heights Company. In the late 1940's and again in 1951 and 1953, the engineering partnership rendered services to Kensington with respect to the so-called Waring Ranch property in the form of surveying the land, preparing boundary, topographical and master plan maps thereof, and representation before the City of San Diego Planning Commission and other city departments in its efforts to have the land annexed to the City of San Diego so as to make it more salable. Four hundred acres were annexed in 1951 and subsequently sold by Kensington. An additional 1,300 acres were annexed in 1952 or 1953 and sold by Kensington to Bollenbacher & Kelton, Inc., subdividers and developers. The engineering partnership was then employed by Bollenbacher & Kelton, Inc. to do the engineering work on the subdivision and development of the 1,300 acres.

"In 1953, efforts were made by Kensington to have the City of San Diego annex the remaining 4,500 acres. At the time of the annexation proceedings, the engineering partnership prepared a master plan of the area, which indicated the lines along which development might feasibly proceed. The City of San Diego annexed the 4,500 acres in December of 1953. The 4,500 acres contained a lake, some canyons, and a mountain rising about 1,100 feet above the surrounding terrain.

"Shortly before the annexation, Kensington sought Freeland's help in finding a buyer for the 4,500 acres. Freeland contacted several clients who were not interested because they thought that development and subdivision of the area was too remote in time.

"In April 1954, Kensington gave Freeland a verbal option on the land. Freeland and one of his developer-clients, Sam Berger, decided to form a partnership to purchase the land. On August 6, 1954, they entered into an agreement to form the partnership, the terms of which were to be reduced to writing in the near future. Under the agreement, Berger was to enter into an escrow in his own name for the purchase of the land from Kensington. Before the close of the escrow, Berger was to nominate the partnership to take title to the land.

Berger negotiated the terms for the purchase with Kensington. In the course of the discussions, Berger indicated that the whole 4,500 acres would be developed as soon as possible and that he had $20,000,000 in financing available, which was not in fact the case. Berger also told Kensington that the purchase price would be paid off in about three years.

"On August 6, 1954, Berger entered into an escrow agreement with Kensington. The agreement provided for a total consideration of $4,676,666.66 (computed on the basis of $800 per acre plus interest 3⅓ percent), payable $100,000 down and the balance in 20 annual installments. The purchase price was to be evidenced by an in-

stallment promissory note, the first installment of $180,000 to become due on August 6, 1955, with the remaining installments due annually thereafter in increasing annual amounts of $6,000 until the 19th installment in the amount of $288,000. The 20th and final installment was to be the remaining balance of $130,666.66. The escrow agreement contained provisions for the release of 150 acres against each annual payment, for the privilege of prepayments with appropriate adjustments for interest, and for the deposit by the purchaser of $200,000 to be disbursed for off-site improvements upon instruction from Kensington.

"The term 'off-site improvements' comprehended two things: (a) the bringing of utilities, viz., water, sewer, gas, electricity, and telephone, from a point distant from the boundaries of the property being developed up to the boundaries of such property; and (b) the installation of a utility, e.g., a water main, on the property being developed, which utility is larger than required to serve such property but which is nevertheless required by the City of San Diego in order to be available to serve further outlying property in the path of future development. With regard to these latter 'off-site improvements,' the city generally paid the difference between what the property being developed required and what the city insisted upon for purposes of future property development.

"Freeland provided $70,000 towards the $100,000 down payment. Berger borrowed the other $30,000 with Freeland acting as guarantor of the loan.

"In the process of trying to raise the $200,000 deposit, Freeland contacted the General Petroleum Corporation, seeking a loan. As part of the attempt to borrow the funds, a letter was sent on September 14, 1954, over Freeland's signature, but without identification as to the capacity in which he was signing, to General Petroleum Corporation's representative in San Diego. The letter proposed that the corporation lend the necessary funds in exchange for exclusive service station sites within the contemplated 4,500-acre development. The letter also stated that a master plan for the development of the entire 4,500 acres was being completed and that it was proposed to start immediately the development of approximately 2,000 homes. The letter further stated that it was anticipated that a minimum of 4,000 homes would be constructed and occupied within three years and that, after the points involving financing the off-site improvements, completing the master plan, and selecting the location of the first 2,000 homes had been settled, consideration would be given to the sale of acreage to subdividers capable of proceeding with the development in a satisfactory fashion. After due consideration, General Petroleum declined to provide any funds.

"After several unsuccessful attempts to raise the $200,000 from various other sources, Berger's associates in a development operation consisting of a joint venture of several corporations, known as 'Country Club Park' (for which Freeland individually acted as a consultant before various governmental agencies), agreed to put up the $200,000

for the off-site improvements. In return, this group (hereafter referred to as the 'Barenfeld-Glaser Group') received a 20 percent interest in the Berger-Freeland partnership.

"On October 21, 1954, the Lake Murray Development Company, a California corporation (hereinafter referred to as 'LMDC'), was incorporated for the purpose of subdividing and developing land and constructing homes thereon. LMDC was capitalized with funds that were advanced by the Barenfeld-Glaser Group. The stock of LMDC was held by Herbert Glaser, an attorney, as trustee for the benefit of the corporations which comprised the Country Club Park joint venture. Berger was the initial president of LMDC and Herbert Glaser was its secretary and attorney. Neither Freeland nor Lowthian was an officer, director, stockholder, or investor in LMDC. Other principals included Sam Glaser, the father of Herbert, and Jack Barenfeld.

"Shortly after October 21, 1954, but prior to October 26, 1954, Sam Glaser and Jack Barenfeld caused $200,000 to be advanced by the Country Club Park joint venture to LMDC and thence from LMDC to the Berger-Freeland partnership, San Berger Investment Company (hereinafter referred to as 'SBIC'). On October 25, 1954, SBIC caused the $200,000 to be deposited in the escrow covering the purchase of the 4,500 acres. On October 26, 1954, the escrow was closed and title in the land was vested in SBIC subject to a deed of trust for the unpaid purchase price.

"On or about October 26, 1954, SBIC and LMDC entered into an option agreement, which

was subsequently reduced to writing and executed on November 23, 1954. Partial consideration for this option was the fact that Sam Glaser and Jack Barenfeld had caused LMDC to provide the $200,000 to SBIC to enable it to close the escrow. The agreement gave LMDC an option to purchase 500 acres of land lying within a larger parcel of approximately 800 acres in the southeast corner of the property for a price of $2,000 per acre. The option agreement further provided in pertinent part:

"(a) That SBIC was to release from the Kensington escrow a minimum number of acres per year in order to prevent a lapse of its right to continue to release acreage.

"(b) That if LMDC purchased less than 150 acres per year under its option, SBIC had the right to sell the unpurchased difference.

"(c) That LMDC realized that SBIC had an oral arrangement with 'other subdividers' to purchase portions of the 800-acre parcel within which the 500 acres subject to the option was encompassed.

"(d) That SBIC would cooperate with LMDC in filing the necessary maps and in expeditiously completing the building lots.

"(e) That LMDC would submit to SBIC all its contracts with subcontractors for all items of work so as to guarantee that the cost would not exceed a certain minimum.

"(f) That LMDC should be reimbursed by SBIC for expenses in excess of the stipulated maximum per lot cost of development, and SBIC would

retain, as profit, any funds remaining in the trust fund established for lot development.

"(g) That SBIC would be liable for all off-site improvement costs in excess of the $200,000 originally advanced by LMDC.

"On November 23, 1954, the date on which the option agreement between SBIC and LMDC was signed, a formal limited partnership agreement was also executed by all of the general and limited partners in SBIC. This agreement was effective as of August 6, 1954. Under the terms of the agreement, Freeland, with a 32 percent interest, and Berger, with a 20 percent interest, were the general partners. Lowthian, with an 8 percent interest, was Freeland's designee and was a limited partner. The HAB Trust and the MLB Trust, each with a 10 percent interest, were Berger's designees and were limited partners. The final 20 percent was a limited partnership interest held under the name of Lake Murray Trust No. 1. The interests of the HAB Trust and the MLB Trust in SBIC were created by Sam Berger for his two sons, Harvey A. Berger and Marshall L. Berger. Sam Berger was the sole trustee of the HAB Trust and the MLB Trust. Neither the beneficiaries of these trusts, Harvey A. Berger and Marshall L. Berger, nor the trusts themselves held any interest in LMDC. The 20 percent interest in SBIC, held under the name of Lake Murray Trust No. 1, was established for the benefit of Jack Barenfeld and Samuel Glaser. At a later date, Barenfeld and Glaser gave 10 percent of their interest in this trust to the other members of the Barenfeld-Glaser group.

"The preamble to the SBIC partnership agreement provided that the purpose of the partnership was to engage 'in the business of buying, selling and developing land upon the real property commonly known as the Third Annexation of the Waring Property consisting of approximately four thousand five hundred (4500) acres of land in the City of San Diego, State of California.'

"The body of the agreement provided, *inter alia:*

"(a) That the term of the partnership would be 10 years.

"(b) That each partner, general or limited, was prohibited from selling, assigning, or transferring his interest in the partnership to any person other than another partner but that the agreement would subsequently be amended to resolve the question of the withdrawal or sale by the partners of a partnership interest.

"(c) That Freeland and Berger were to contribute $70,000 and $30,000, respectively, to the partnership but further that they could withdraw said sums from the first monies available to the partnership.

"(d) The general business policy of said partnership in all questions relating to the management of its business should be determined by the mutual consent of the general partners.

"(e) Both general partners were to have full management rights and control.

"(f) Freeland was to receive an engineering fee of $25 per lot (in addition to any other engineering fees) from the first 2,000 lots 'developed or sold by the partnership to third parties.'

"(g) That in the event the general partners could not agree, the problem would be submitted to arbitration.

"After the closing of the Kensington escrow on October 26, 1954, Berger was anxious to get LMDC activated. The engineering partnership and Freeland, as consulting engineer for LMDC, commenced applying for the necessary permits and talking with various city departments in order to get necessary city approval. Freeland's engineering partnership was also employed by LMDC and performed various services for LMDC relating to on-site development and off-site improvements.

"On November 8, 1954, Freeland forwarded to the San Diego Planning Commission on behalf of LMDC a 'Tentative Map Unit No. 1 [Lake Park Development Property].' Unit No. 1 consisted of approximately 50 acres to be subdivided into approximately 260-280 lots. Submitted at the same time were ten copies of a master plan map for the entire 4,500 acres and ten copies of a master plan map of the 800 acres subject to LMDC's 500 acre option. The master plan map of the 4,500 acres was an identical copy of that prepared for Kensington and Mrs. Waring on October 23, 1953, except that a portion of the lower right-hand section of that map had been cut out and a new sec-

tion representing Unit No. 1 inserted. The map for the 4,500 acres indicated tentative locations for schools, parks, and supermarkets for the entire tract. It showed that, when fully developed, the 4,500 acres would yield an estimated 16,000 lots. As a result of discussions with representatives of SBIC and LMDC concerning approval of the subdivision plan, the representatives of the San Diego Planning Commission understood that Unit No. 1 was the first unit in a planned development that would ultimately total 4,500 acres.

"On November 4, 1954, LMDC purchased 3.19 acres by a partial exercise of its 500 acre option. LMDC then commenced construction of seven model homes on this acreage. It was necessary for LMDC to bring off-site improvements to the Lake Park Property's southeast border in order to develop this acreage. In late December 1954, the seven model homes were completed and opened to the public for inspection. The advertising campaign referred to a 'City of Tomorrow' to be developed on the 4,500 acres. Freeland, though he was aware of such advertising, disapproved of it and so informed Berger.

"On December 14, 1954, the City Council, on the recommendation of the Planning Commission, gave preliminary approval to the subdivision plan for Unit No. 1. Prior to December 23, 1956 [*sic*], LMDC, through its agent Freeland, submitted to the City Planning Department a tentative subdivision map for Units Nos. 2 and 3. Prior to January 17, 1955, LMDC similarly submitted a tentative subdivision map for Units Nos. 4 and 5. The size of the lots ranged between one-fourth of an acre and

one-fifth of an acre. It was anticipated that 500 acres would produce between 2,200 and 2,400 lots. Units Nos. 1 through 5, if fully developed, would contain a total of approximately 3,000 lots and covered the 800-acre parcel on which LMDC had a 500-acre option.

"The City, in considering a tentative subdivision plan, was concerned, *inter alia,* with the location and adequacy of schools, parks, shopping centers, and off-site improvements, including adequate water supply. Though an immediate proposal might concern only a very small number of acres, the city considered the development in terms of overall plans for the surrounding area. The city would not permit wasteful duplication of facilities such as two small water reservoirs where one larger reservoir would be considerably more economical.

"Both Berger and Freeland represented SBIC in negotiations with the San Diego Unified School District pertaining to the granting of options for school sites within Units 1 through 5.

"On March 8, 1955, SBIC, through a letter signed by Berger, offered the School District school sites at a price equal to $2,000 per acre plus 'the average off-site cost for the entire 4,500 acres of approximately $200 per acre, plus the cost of on-site improvements. Additonal land for park and recreational purposes was offered on the same terms. This offer was not accepted by the School District. On September 23, 1955, SBIC, through a letter signed by Berger, offered the School District, for $1 each, options on school sites within Units 1 through 5 at $1,900 per acre for usable

land. SBIC also agreed to give the School District renewable options on specific sites of land selected by the School District on the remaining areas to be developed by SBIC.

"On July 26, 1955, the San Diego City Council adopted the Final Subdivision Map of College Ranch Unit No. 1, which map was filed and recorded in the County Recorder's Office on July 27, 1955. On July and August of 1955, LMDC partially exercised its 500-acre option and purchased an additional 146.93 acres from SBIC. LMDC then commenced development of Unit No. 1. LMDC also commenced the off-site improvement work for the 500-acre development. The principal aim in construction of these facilities was to provide adequate facilities for the 500 acres with minimum damage to the remaining 4,000 acres.

"In December 1954 or January 1955, a series of disputes arose between SBIC and LMDC. As a result of those disputes, LMDC and SBIC entered into an amended option agreement covering the 500 acres. The purchase price of the land was changed to $2,000 per acre for the first 250 acres and $1,800 per acre for all additional acreage. The 'loan' of $200,000 by LMDC to SBIC was labelled a 'credit,' with LMDC entitled to recover any portion not used for off-site improvements, and no interest would be paid on the credit. LMDC's prior oral agreement to pay Freeland $25 per lot for his personal service and counsel was reduced to writing. The agreement also eliminated the lot and off-site improvement cost guarantees by SBIC.

"LMDC engaged in the construction of 196 homes. By the summer of 1955, LMDC developed financial difficulties. In an attempt to remedy the situation, Berger sought a change in the amended option agreement permitting LMDC to acquire what he thought would be more salable land. He proposed to develop land in the foothills of the mountain which would have a view of the lake. Employees of the engineering partnership prepared a feasibility study of the proposal, the conclusion of which was that the cost of off-site improvements would be prohibitive at that time.

"Ultimately, LMDC was unable to overcome its financial difficulties. It became insolvent on May 4, 1956. LMDC assigned to Phoenix Insurance Company of Hartford all of its assets, except that it retained the right under the amended option agreement to purchase 200 acres of land out of the 500 acres originally covered by the option. Since LMDC had already exercised its option to the extent of approximately 150 acres, the portion of the option assigned to Phoenix only covered the right to purchase the remaining approximately 150 acres. Phoenix subsequently exercised this option.

"Berger was blamed for mismanagement of LMDC and was himself in financial difficulty. In August 1956, Carlos Tavares, representing a group of developers, including himself, approached Berger and offered to purchase his interest in SBIC. Tavares had been one of the developers approached by Freeland at the time of the annexation of the 4,500 acres.

"On August 10, 1956, the Tavares group agreed to buy out Berger's interest and the respective 10 percent interests of the HAB Trust and the MLB Trust in SBIC for $950,000. Berger did not get Freeland's consent for the sale of his interest in SBIC as required by the partnership agreement.

"Tavares then approached Freeland in an effort to purchase his interest in SBIC or, in the alternative, to have Freeland join the Tavares group in the development of the SBIC land. Freeland told Tavares he was not interested in joining in the development and decided to sell out. Lowthian decided to sell out her interest as well. Freeland received $730,000 for his interest, while Lowthian received $220,000 for hers. In the agreement of sale, they consented to the purchase from Berger.

"During the taxable periods portions of the acreage were utilized for grazing and the raising of barley. The partnership reported gross income from these sources in 1955 of $10,467.99 against total expenses of $27,609.92 (of which $15,319.51 represented real estate taxes) and in 1956 of $17,958.50 against total expenses of $45,032.69 (of which real estate taxes represented $15,619.01).

"Freeland did not wish directly to engage in subdividing and developing the land, either individually or through any other business form, because it would place him in competition with his clients and those of his engineering partnership and thus be financially injurious.

"At no time material hereto was either Freeland or Lowthian individually a dealer in real estate or

individually holding real estate for sale to customers in the ordinary course of business.

"Although no improvements were made directly to the acreage not covered by the option to LMDC, the entire tract benefited from the off-site improvements made by LMDC. SBIC itself never directly advertised, promoted, or otherwise engaged in active efforts to solicit for its land, nor did it authorize anyone to undertake such activities directly on its behalf.

"Freeland, on behalf of SBIC, refused several unsolicited offers for the sale of portions of the acreage not covered by the LMDC option.

"SBIC never purchased any real property except the 4,500 acres here in issue. The only sales of real property ever made by SBIC, aside from the 300 acres acquired under the 500-acre option to LMDC, were (1) the sale of a fractional acre to the telephone company and (2) the sale of approximately four acres to the City of San Diego for a reservoir site as required by Kensington when SBIC purchased the land. The only other land transactions of SBIC involved the grant to the San Diego School District of options to purchase sites within the area to be developed by LMDC for three elementary schools and one junior high school. SBIC also agreed to grant further similar options to the School District when development proceeded beyond the initial 500 acres. At the time of the annexation of the 4,500 acres, the city had required the then owners to agree to sell school sites within the property, and Kensington passed this obligation along to SBIC." C.T. 116-33 (footnotes omitted).

On the basis of these facts the Tax Court further found that SBIC held its land "primarily for sale to customers in the ordinary course of [its] trade or business." This finding was made in spite of contentions by petitioners that the land was held only for "investment" purposes. It was recognized by the court that none of the "normal criteria" relevant to questions such as the one involved here—for instance, frequency and continuity of sales, advertising, solicitation, extent of development and the like—could be relied upon in this instance to establish a purpose to sell to customers. The opinion went on, however, to state that:

> "The normal criteria are not the exclusive benchmarks for decision in a case such as this, where there were good reasons for indirect as opposed to direct participation in development activities and where the period of gestation was prematurely cut short." C.T. 146.

The court relied instead upon a theory of "indirect participation" in sales and development activities:

> "We think it clear that SBIC did not itself intend to develop the 4,500 acres—such action would have been damaging to Freeland's professional activities and those of his engineering partnership. But it is equally clear that the ultimate success of the venture, upon which SBIC had embarked, was dependent upon insuring the development of the acreage by someone. . . .
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> ". . . .
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> ". . . We think that from the beginning, the partners in SBIC intended to sell off the property as quickly as the area could be made ready for de-

velopment and that to this end they planned actively and continuously to participate in sequential development efforts. LMDC was the primer for the entire project. It was the first vehicle to be utilized and the partners of SBIC were deeply involved in the activities of that entity. Cf. *Ackerman v. United States,* 335 F.2d 521 (C.A. 5, 1964). Respondent suggests that LMDC was to be the sole vehicle of the partners, transferring its activity from one segment of the tract to the next as soon as the development of the previous segments was completed. We do not find it necessary to go that far. It is enough for us to say that the partners would seek constantly to construct vehicles for development, in which they would probably participate in one form or another, in order to be in a position to sell the acreage involved in slices of varying sizes as promptly as possible. Alternatively, they were ready to sell at any time that the partnership received acceptable offers. Cf. *James E. Kesicki,* 34 T.C. 675 (1960)." C.T. 139, 146-47.

Three points should be made initially in connection with our consideration of this general finding. First, if it was properly made, then the petitioners' joint challenge to the Tax Court's legal conclusions must be rejected. Assuming that the nature of SBIC's business was in fact what the Tax Court found it to be—that is, that the partnership's purpose was to have the land in question developed—then it would be immaterial that the partnership sought to utilize a legally separate entity, LMDC, in order to achieve its commercial ends.

Cf. Ackerman v. United States, 335 F.2d 521 (5th Cir. 1964); and *Tibbals v. United States,* 362 F.2d 266, 271-72 (Ct. Cl. 1966), in which development activities of taxpayer-controlled close corporations, relating to land previously transferred to the corporations by the individual taxpayers involved, were held attributable to those taxpayers. (Indeed, in *Ackerman* the transfer was made indirectly—first to a trust and only later to the corporation.) In cases such as this, as in a great many situations, "the tax law deals in economic realities, not legal abstractions. . . ." *Commissioner v. Southwest Exploration Co.,* 350 U.S. 308, 315 (1956). Second, as with all findings of fact, we are compelled to uphold the trial court unless the finding at issue is "clearly erroneous." *E.g., Rollingwood Corp. v. Commissioner,* 190 F.2d 263, 265 (9th Cir. 1951). And third, the evidence should be scrutinized in light of the fact that the burden of proof in the Tax Court was on petitioners. Tax Ct. R. 32; *Factor v. Commissioner,* 281 F.2d 100 (9th Cir. 1960), *cert. denied,* 364 U.S. 933 (1961). With these considerations in mind, we find ourselves unable to uphold petitioners' contentions.

There was sufficient evidence, first of all, to support a finding that the original purpose of SBIC was that attributed to it by the Tax Court. That evidence includes Berger's sweeping statements concerning imminent development of the entire tract; similar language in the letter to General Petroleum; the requirement in the contract with Kensington that SBIC deposit $200,000 in escrow for off-site improvements, which the Tax Court reasonably viewed as "mirror[ing] the vision of development which the parties, including SBIC, had in

mind," C.T. 139; the increasing amounts of the yearly payments required of SBIC under that contract, indicating (the Tax Court was entitled to find) that development may have been intended to be the source of repayment funds; the "interlocking" nature of SBIC and LMDC membership; the provisions in the original SBIC-LMDC contract which in effect passed some of the latter's risks and opportunities for profit in development activities on to SBIC; the discrepancy between the $1037 per acre paid SBIC and the $2000 per acre it immediately received from LMDC (which, though certainly explicable in part on other grounds, was not unreasonably taken to represent to some extent "a method of siphoning off to the common participants in SBIC and LMDC a portion of the latter's profit hopefully as long-term capital gains," C.T. 144; and the fact that the off-site improvements to be provided out of the $200,000 deposited by LMDC could be viewed as "not only . . . for the benefit of the initial 500-acre tract but also [for the indirect benefit of] the remaining acreage," C.T. 144-45.

True, the inferences drawn from some of these facts were not required inferences, and there was evidence in petitioners' favor with regard to many issues. The Tax Court might possibly have properly found in petitioners' favor. It may in fact be that no one piece of evidence in itself would support that court's finding. In combination, however, the factors referred to above provide a substantial basis for the finding of SBIC's original purpose regarding the land.

Petitioners contend, however, that the relevant intent for purposes of the issue here raised is that held immediately prior to sale. *See Tibbals v. United States,*

362 F.2d 266 (Ct. Cl. 1966). And they vigorously urge that even if the purpose found by the Tax Court may be attributed to SBIC at the outset of its operations, that purpose changed in light of later events. They point, first, to the disputes that occurred between SBIC and LMDC; second, to the failure of LMDC, and third, to the sale of Berger's interest in SBIC to Tavares.[2]

Petitioners' contentions here are admittedly not without support. There would perhaps have been considerable basis for a finding that SBIC's original purpose changed after the occurrence of these events. The nature of the questions is such, however, as to make it difficult for us to rule in accord with petitioner's contentions. As a general matter, first of all, courts should be wary of finding that, because of a lack of business success, the purpose for which property is held changes from one of sale to customers to one of investment. The clear purpose of denying capital gain treatment to profit attributable to the sale of inventory is to prevent the owners of businesses yielding ordinary income from in effect reducing their tax liability on such income merely by selling their businesses *in toto*. This purpose would in many instances be frustrated if an intention to "liquidate" such a business sufficed to establish the sort of "change of purpose" which petitioners contend occurred here. Moreover, "intent" is, particularly when applied to an impersonal entity such as a partnership, to a great extent a fiction—or, perhaps more accurately, a legal construct. It is quite con-

[2]This issue—which we resolve against petitioners—is considered although it is not at all clear that it was raised before the Tax Court. The Commissioner has not specifically urged that we refuse to consider it on that ground.

ceivable that, particularly after the failure of LMDC and the entry into SBIC of Tavares (who wanted to develop the land directly), SBIC's "purpose" regarding the land was to some degree not clearly defined. Freeland did not want to involve himself directly in development activities, yet the instrument which the partnership had chosen to use as a means of engaging in "indirect" development—LMDC—no longer existed, and one of the original partners, Berger, was in financial difficulties. Courts must, however, often decide questions which are thus speculative in nature. And, considering (1) the supported finding that SBIC had at first intended to develop the land indirectly, and (2) the fact that the burden of proof was on petitioners, this court cannot conclude that it was "clearly erroneous" for the Tax Court to find that the partnership's purpose had not changed. We cannot hold as a matter of law that that purpose *must* have changed.

Two further issues are raised by petitioner Lowthian. She contends, first of all, that the "intent" of the partners engaged in indirect development activities through LMDC ought not to be attributed to her. For her, she argues, the SBIC venture was merely an "investment." This latter assertion may, of course, be true. But it is the intent of the partnership, and not of any individual partner, that is in issue according to the Internal Revenue Code. Under the written partnership agreement, to which petitioner Lowthian was a party signatory, the business policy of SBIC was to be determined by the general partners, Berger and Freeland; Lowthian, as a limited partner, thus agreed that she should have no hand in determining that purpose. The case of *United States v. Rosebrook*, 318 F.2d 316

(9th Cir. 1963), *aff'g* 191 F.Supp. 356 (N.D. Cal. 1960), cited by petitioner, is inapposite. There, the taxpayer sold a one per cent interest in land which had originally been purchased by her father in the name of a trust having her as beneficiary. Although the interest had been committed to a joint venture, it was directly owned by the taxpayer who was a tenant in common; under section 1221 of the Code, therefore—and especially since she had succeeded involuntarily to ownership of the land and participation in the joint venture—the court looked to her purpose rather than to that of other participants in the venture, and ruled that she had held the land as an investment. Here, both essential elements of the factual situation in *Rosebrook*—direct ownership and involuntary participation in the joint scheme—are absent. Petitioner's tax liability is clearly governed by the purpose of the partnership.

Finally, petitioner Lowthian contends that the Commissioner abused his discretion in reopening with respect to her 1956 liability. The Commissioner asserts that he acted under Rev. Proc. 59-25, 1959-2 Cum. Bull. 938 (since superseded by Rev. Proc. 63-9, 1963-1 Cum. Bull. 488, and Rev. Proc. 64-40, 1964-2 Cum. Bull. 971), which states:

> "It is the administrative practice of the Internal Revenue Service not to reopen cases previously closed by the District Director unless there has been substantial error, both in amount and in relation to the total tax liability, or there is evidence of fraud, malfeasance, collusion, concealment or the misrepresentation of a material fact."

Pointing out that there is no evidence of "fraud, malfeasance, collusion, concealment or the misrepresenta-

tion of a material fact," and that the Commissioner must therefore have acted under the "substantial error" clause of the provision, petitioner contends that the latter phrase refers not to the substantiality of the amount involved, but to the "obviousness" of the mistake claimed to have been made. Since the factual question here involved is a relatively close one, she concludes that reopening was not authorized. We reject petitioner's proposed construction of the clause, however, not only because it might impose unwise and impractical restrictions upon the Commissioner's power to reopen, but also because the very terms of the provision in question clearly relate "substantiality" to "amount." There is no contention that petitioner Lowthian's deficiency is not substantial in amount, and, indeed, any such contention would be bound to fail.[8]

AFFIRMED.

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[8]The total deficiencies in question in petitioner Lowthian's case amount to $38,763.01. Her deficiency for 1956 is $10,231.29, while the tax disclosed by her return for that year was $4085.34. Although it is not specifically claimed here that the Commissioner's action in reopening with respect to Freeland's liability represents an abuse of discretion, it may be noted that the deficiencies in question in their case total $239,469.78.

Relevant Findings of the Tax Court of the United States Not Quoted in the Opinion Below, Being the Last Two Paragraphs of Said Findings.

During 1957, Internal Revenue Agent George Colling was assigned to audit the 1956 returns of Freeland and Lowthian. Colling specifically questioned the propriety of capital gain treatment of the sale of their respective interests in SBIC. SBIC's books and records were examined, as were many official city records. Colling concluded that Freeland and Lowthian correctly reported the gain from the sale of their respective partnership interests as capital gain. On September 19, 1958, the district director of internal revenue sent letters to Freeland and Lowthian accepting their 1956 returns, subject to adjustments not material herein.

On April 26, 1962, the district director approved the reopening of petitioners' 1956 year "due to the amount of money involved and in the interest of being consistent" with the cases of the other partners in SBIC handled by another agent. On July 29, 1964, respondent issued his statutory notices herein asserting that the sale of the partnership interests resulted in ordinary income. The period of limitations had been extended beyond that date by appropriate consents executed by Freeland and Lowthian.

Order on Petition for Rehearing.

United States Court of Appeals for the Ninth Circuit.

Estate of Eugene L. Freeland, Deceased, by Security First National Bank, a national banking association, Executor, and Vera Good Freeland, by L. N. Turrentine, Conservator, *Petitioners,* vs. Commissioner of Internal Revenue, *Respondent.* No. 21,795.

Margaret C. Lowthian, *Petitioner,* vs. Commissioner of Internal Revenue, *Respondent.* No. 21,795-A.

[May 6, 1968]

Before: BARNES, JERTBERG and ELY, Circuit Judges

Upon petition for rehearing, the following changes are ordered made in the original opinion, filed March 8, 1968:

1. On page 6 of the slip opinion, line 4, the word "at" is ordered inserted between the word "interest" and the numeral "3 1/3."

2. On page 18, line 14, the comma after the abbreviation "LMDC" is ordered changed to a semicolon.

3. The first six sentences of the paragraph beginning at line 16 of page 18 are ordered stricken, and the following ordered inserted in their place:

> "Petitioners' contentions admittedly are not wholly without support. There perhaps would have been some basis for a finding that SBIC's original purpose changed after the occurrence of these events. The nature of the question is such, however, as to make it difficult for us to rule in accord with petitioners' contentions. As a general matter, first of all, courts should in situations such as that involved here be wary of finding

that, because of a lack of business success, the purpose for which property is held by a partnership changes from one of sale to customers to one of investment. The clear purpose of section 751 is to prevent members of partnerships from reducing their tax liability by converting potential ordinary income—attributable to inventory or unrealized receivables—into capital gain by selling their partnership interests. *Roth v. Commissioner*, 321 F.2d 607, 611 (9th Cir. 1963), and sources cited therein. This purpose would in many instances be frustrated if partners' decisions to sell their interests necessarily sufficed to establish the sort of 'change of purpose' which petitioners contend occurred here."

The paragraph then continues with the seventh sentence, beginning, "Moreover, . . ."

4. The last two sentences of the final paragraph on page 20 are ordered stricken, and the following ordered inserted in their place:

"We reject petitioner's proposed construction of the clause, however, not only because it might impose unwise and impractical restrictions upon the Commissioner's power to reopen, but also because the very language of the provision in question clearly defines 'substantiality' in terms of 'amount' and 'relation to the total tax liability.' There is no contention that petitioner Lowthian's deficiency is not substantial in either respect, and, indeed, any such contention would be bound to fail.[8]"

Other than as hereinabove set forth, the opinion is not modified.

As so modified, the opinion stands, and the petition for rehearing is denied.

Motion for Reconsideration of the Petition for Rehearing.

In the United States Court of Appeals for the Ninth Circuit.

Estate of Eugene L. Freeland, Deceased, by Security First National Bank, a national banking association, Executor, and Vera Good Freeland, by L. N. Turrentine, Conservator, Petitioners, vs. Commissioner of Internal Revnue, Respondent. No. 21,795.

Petitioners now move court, because of the modification of its opinion, to reconsider its petition for rehearing.

We pass for this purpose the nature and effect of the modification made by the first two of the inserted sentences, since the entire insert is made dependent upon the final sentence thereof, and that sentence is clearly unsupported by any finding or evidence. What happened on August 10, 1956, the sale by Berger alone of his partnership interest—the critical and latest event relied on by petitioners as resulting in change of purpose—is not, as to petitioner Freeland, the equivalent of what this Court assumes, "partners' decisions to sell their interests."

As this Court's opinion shows, slip opinion pp. 13-14, Berger, then in financial difficulty, did not even get Freeland's consent to his sale as required by the partnership agreement. Furthermore, as this Court's opinion there also shows, it was only after Tavares had so purchased Berger's interest, that he tried to buy Free-

land's, but, as shown in our opening brief, at p. 8, citing Tavares' deposition, pp. 10-12, Tavares had difficulty even in getting a price.

Clearly then, what happened on August 10, 1956, although it radically altered SBIC in respect to the land, —so that, as shown in our petition for rehearing, at pp. 3-4, the purpose of holding afterward could not be tied to the purpose before,—did not include a decision, or even a plan, of Freeland to sell his interest. As a result, the sentences now inserted by this Court in its opinion are unsupported by any finding or any evidence of such a decision at that time. It would follow then from this Court's own opinion as modified that petitioners should be sustained.

If a hearing on this motion is granted, petitioners suggest May 14, 1968, or any later date convenient to the Court.

Respectfully submitted,

George T. Altman
Attorney for Petitioners

Testimony Cited in Motion for Reconsideration of the Petition for Rehearing But Not Referred to in the Tax Court's Findings, Being the Testimony Contained in Deposition of Carlos Tavares, p. 10, Line 19, to p. 11, Line 26.

Q. After you had purchased Mr. Berger's partnership interest, did you negotiate with any of the other partners of the Sam Berger Investment Company?

A. As soon as I got Sam Berger nailed down, I approached Gene Freeland.

Q. You approached him?

A. Yes.

Q. Did you have any difficulties in your negotiations with Mr. Freeland?

A. Had a lot of difficulties.

Q. In what regard?

A. Well, I have known Gene, Mr. Freeland, for a long time. He's been my engineer for a long time. He still does my work, him and Peterson, and in spite of the fact of our close relationship with the Freeland-Peterson office, I had a lot of difficulty in getting a price from them and also I had a lot of difficulty in dealing with him.

Q. Would you say that Mr. Freeland was anxious to sell his interest in the partnership?

A. No, he was awfully hard to get. As a matter of fact, Mr. Kockritz, who is doing business with him, I told Mrs. Kockritz that Mr. Kockritz was the greatest no-good guy in the world. I have never bought a piece

of property from anybody when the terms were so difficult. We actually paid Freeland cash for the whole amount. We gave him cash plus putting up second trust deeds as collateral so that in actual fact he got all cash for his piece of property.

Q. Did you ever suggest to Mr. Freeland that he go into the development business with you rather than your buying out his interest in that land?

A. Oh, sure.

Q. And was Mr. Freeland interested in so doing?

A. No, wasn't interested at all.

Order Denying Said Motion.

In the United States Court of Appeals, for the Ninth Circuit.

Estate of Eugene L. Freeland, Deceased, by Security First National Bank, a national banking association, Executor, and Vera Good Freeland, by L. N. Turrentine, Conservator, Petitioners, vs. Commissioner of Internal Revenue, Respondent. No. 21795.

ORDER

On Motion for Reconsideration of
The Petition for Rehearing

Before: BARNES, JERTBERG and ELY, Circuit Judges

The motion for reconsideration of the petition for rehearing is denied.

Stanley N. Barnes
United States Circuit Judges



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In the Supreme Court of the United States

OCTOBER TERM, 1963

ESTATE OF EUGENE L. FREELAND, DECEASED, BY SECURITY FIRST NATIONAL BANK, A NATIONAL BANKING ASSOCIATION, EXECUTOR, ET AL.

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

ERWIN N. GRISWOLD,
Solicitor General,

MITCHELL ROGOVIN,
Assistant Attorney General,

WILLIAM A. FRIEDLANDER,
MARCO S. SONDERSCHEIN,
Attorneys,
Department of Justice,
Washington, D.C. 20530.

In the Supreme Court of the United States

OCTOBER TERM, 1968

No. 341

ESTATE OF EUGENE L. FREELAND, DECEASED, BY SECURITY FIRST NATIONAL BANK, A NATIONAL BANKING ASSOCIATION, EXECUTOR, ET AL.

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

The ultimate issue here is whether or not Eugene L. Freeland[1] and Margaret C. Lowthian ("petitioners") are entitled to capital gain treatment on their sales in November 1956 of their respective partner-

[1] Mr. Freeland has died since the transaction here in issue, and his interest is now represented by his estate. His wife, Vera G. Freeland, represented by a conservator, is a party because joint returns were filed for the years in question.

ship interests in the Sam Berger Investment Company (SBIC). Because Section 751(a) of the Internal Revenue Code holds that the gain "attributable to * * * inventory items of the partnership which have appreciated substantially in value" shall be taxed as ordinary income, the Tax Court's decision turned on its finding that the real estate which comprised the partnership's basic asset was being held for sale to customers at the time petitioners sold their interests.[2]

Mr. Freeland, with a 32% interest, was one of two general partners, and Miss Lowthian, Freeland's private secretary in his civil engineering practice, held a limited partnership share of 8% in SBIC. Freeland and one of the clients of his engineering firm, Sam Berger, a real estate developer, formed SBIC to purchase 4500 acres of land near San Diego, California. The total sales price was $4,676,666.66 (computed on the basis of $800 per acre plus interest at 3⅓%), payable $100,000 down and the balance in 20 annual installments. The contract of sale required an escrow of $200,000, to be used for off-site improvements such as bringing water, gas, and other utilities from a distant point. After several unsuccessful attempts to raise the $200,000 escrow money from other sources, Berger's associates in another development corporation agreed to put up the $200,000. In return, these associates received a 20% interest in SBIC. (Pet. App. 5-12.)

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[2] Sections 751(d)(2)(A) and 1221(1) define "inventory" to include "property held * * * primarily for sale to customers in the ordinary course of" the business.

Shortly after SBIC purchased the land, the Lake Murray Development Company (LMDC), was incorporated for the purpose of subdividing and developing land and constructing homes thereon. The SBIC partners other than petitioners held all the stock of LMDC; Berger was its president. SBIC gave LMDC an option to purchase 500 acres of SBIC's land at $2000 per acre. The option provided, *inter alia*: (1) that LMDC would submit to SBIC all its contracts with subcontractors for all items of work so as to guarantee that the cost would not exceed a certain minimum; and (2) SBIC would be liable for all off-site improvement costs in excess of the $200,000 advanced by LMDC. (Pet. App. 10-12.)

Plans for subdividing 50 acres, as well as a master plan for the entire 4500 acres, were submitted to the San Diego Planning Commission. LMDC exercised part of its option and also began the off-site improvement work for the 500 acre development. A series of disputes between LMDC and SBIC arose and as a result, LMDC and SBIC entered into an amended option agreement covering the 500 acres. The price of the land was changed to $2000 for the first 250 acres and $1800 per acre for all additional acreage. Also, SBIC's guarantee of off-site improvement costs was eliminated. (Pet. App. 14-17.)

LMDC constructed 196 homes, but by the summer of 1955 was in financial difficulties. On May 4, 1956, LMDC became insolvent. Berger was also in financial difficulty and sold his 20% interest in SBIC plus the 10% interests of two trusts of which he, Berger, was trustee to Carlos Tavares and his asso-

ciates (the Tavares group) on August 10, 1956. Tavares then sought to purchase Freeland's share or, in the alternative, have Freeland join his group in the development of the SBIC land. Mr. Freeland decided to sell out, as did Miss Lowthian. On September 7, 1956, they gave the Tavares group an option to purchase their shares and the sale was consummated shortly thereafter. (Pet. App. 18-19.)

The Tax Court rejected petitioners' contention that the partnership had not conducted activities that are the usual indicia of a holding of land for sale to customers, and ruled that SBIC had done these things indirectly through the agency of LMDC. (Pet. App. 21-22.) Therefore, the Tax Court concluded, the land was being held by SBIC primarily for sale to customers in the regular course of business, and sustained the Commissioner's contention that petitioners' gains should be taxed at ordinary income rates. The court of appeals affirmed.

The courts below have properly applied settled principles of law to the particular facts of this case. The record adequately supports the findings adverse to petitioners. There is no conflict of decisions or any other basis for further review.

1. The evidence summarized in the court of appeals' opinion (Pet. App. 23-24) constitutes an adequate foundation for the Tax Court's finding that SBIC originally held the land with the view of subdiving it and selling it to customers in the ordinary course of business, and petitioners do not seriously argue otherwise. Their principle present contention (see Pet. 4) is that the purpose of holding changed

before their sale of their partnership interests, a position that focuses on several events—particularly Berger's sale of his partnership interest. However, as the court of appeals ruled (Pet. App. 25, 30), although there was evidence that could have supported a finding of a change in purpose, the record by no means compelled the Tax Court to rule that petitioners had sustained their burden of demonstrating such a change. To require such a finding on the present record—which shows no more than a failure of the subdivision enterprise and a desire to liquidate it as evidence of a change in purpose—would too readily permit avoidance of the provisions of law that seek to deny capital gains treatment to profits realized upon the sale of inventory. (See Pet. App. 24-26).

2. We recognize (see Pet. 8-9, 16) that the Court of Claims has determined that several other partners of SBIC were entitled to capital gains treatment on their sales of their interests to the Tavares group. See *Morse* v. *United States*, 371 F.2d 474; *Ginsburg* v. *United States*, decided June 14, 1968 (68-1 U.S.T.C. ¶ 9429). Of course, even if those determinations were based on records that are in all respects identical to the evidence in the present case, it would not be grounds for certiorari, since it would only mean that different finders of fact reached different factual conclusions in cases that could have gone either way. Cf. *John Kelley Co.* v. *Commissioner*, 326 U.S. 521.

The records, at all events, are not as alike as petitioners suggest (see Pet. 8-9). The essential difference is that petitioners sold their partnership interests nearly a year before the sales by the partners

involved in the Court of Claims decisions. The Court of Claims found only that the purpose of holding the land had changed by that later date—October 31, 1967—and did not find it necessary to determine exactly when the change had taken place (see Pet. 9). As the Court of Claims said in *Ginsburg* (slip op., p. 5) there is "nothing in *Freeland* essentially at odds with our decisions in *Morse* and the present cases."

3. Petitioners' other contentions (Pet. 10-15) are in substance an attempt to portray the court of appeals opinion as reflecting a conclusion that petitioners had conclusively demonstrated the required change in SBIC's purpose for holding the land. But at most that court, in making such comments as its observation (Pet. App. 24; see Pet. 10) that the Tax Court "might possibly have properly found in petitioners' favor", was indicating a view that the basic factual question at issue here could have been decided for either side, and that whatever the decision of the finder of fact, the court of appeals would have affirmed. The fact that the evidence could be given another construction or that the evidence would support a conclusion either way does not, as petitioners seem to argue, make the Tax Court's findings clearly erroneous. Petitioners' burden is to show that the evidence cannot support the findings actually made, *United States* v. *Real Estate Boards*, 339 U.S. 485, 495-496; *United States* v. *Yellow Cab Co.*, 338 U.S. 338, 342—something they cannot do.

The petition for a writ of certiorari should be denied.

Respectfully submitted.

ERWIN N. GRISWOLD,
Solicitor General.

MITCHELL ROGOVIN,
Assistant Attorney General.

WILLIAM A. FRIEDLANDER,
MARCO S. SONNENSCHEIN,
Attorneys.

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SUPREME COURT U. S.

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IN THE

Supreme Court of the United States

October Term, 1968
No. 341

ESTATE OF EUGENE L. FREELAND, Deceased, by SECURITY FIRST NATIONAL BANK, a national banking association, Executor, and VERA GOOD FREELAND, by L. N. TURRENTINE, Conservator,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

MARGARET C. LOWTHIAN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

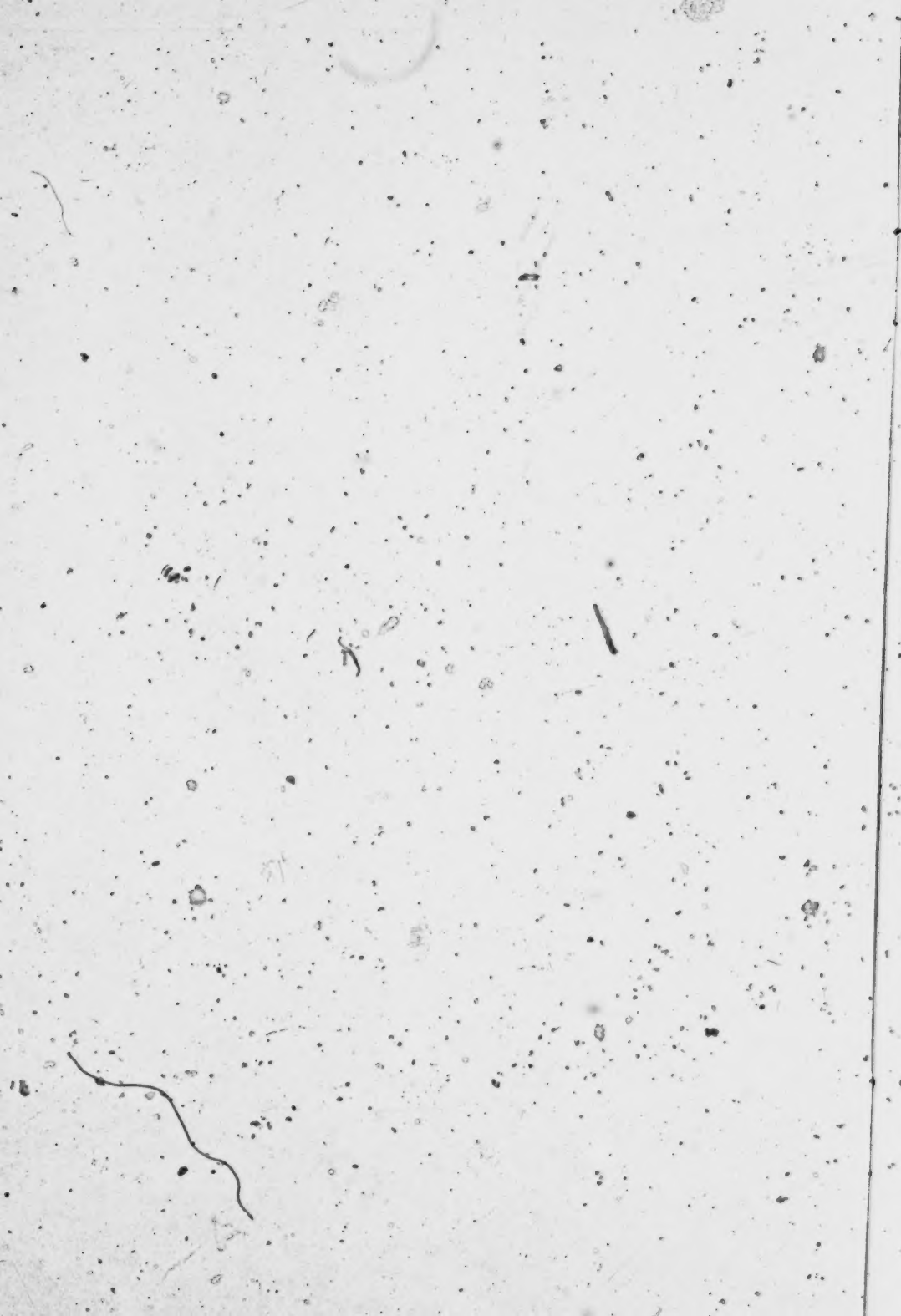
PETITIONERS' REPLY AND SUPPLEMENTAL BRIEF.

GEORGE T. ALTMAN,
424 South Beverly Drive,
Beverly Hills, Calif. 90212,

ADAM Y. BENNION,
523 West Sixth Street,
Los Angeles, Calif. 90014,

Attorneys for Petitioners.

Parker & Son, Inc., Law Printers, Los Angeles. Phone MA. 6-9171.



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IN THE

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vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

MARGARET C. LOWTHIAN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITIONERS' REPLY AND SUPPLEMENTAL BRIEF.

REPLY.

1. Under his point 1, at pp. 4-5, respondent grievously misstates the record. He says that the record "shows no more than a failure of the subdivision enterprise and a desire to liquidate it as evidence of a change in purpose." There was, indeed, "a failure of the subdivision enterprise"; and there was, indeed, "a desire to liquidate it," to liquidate, that is, the *subdivision enterprise.* But that is not all that the record shows. There was also unsubdivided land; and, after Berger's sale of

his interest, on August 10, 1956, the desire of SBIC, the partnership holding the land, was not, except for Berger, to liquidate but to hold. (Pet. App. 34-35.[1]) And there was good reason; the land was in an area of "continuing and substantial appreciation in real estate values." (Pet. App. 5-6.) Clearly if, as respondent contends, SBIC's original purpose was not to hold the land but to subdivide it, then after the failure of LMDC and Berger's agreement to sell his interest in SBIC, the purpose of SBIC, or what was left of SBIC, was no longer to subdivide but to hold.

2. Under his point 2, pp. 5-6, respondent makes reference to the case of *John Kelley Co. v. Commissioner,* 326 U.S. 521. That case, decided in 1946, involving review of Tax Court decisions, applied the limitation on such review which had been established by *Dobson v. Commissioner,* 320 U.S. 489, and had become known as the "Dobson rule." Under that rule review of Tax Court decisions was limited to "clear-cut" questions of law. That limitation, however, was abrogated by Congress in 1948 by a statutory amendment which made the scope of review in the case of Tax Court decisions the same as in the case of decisions of district courts. *United States v. Snyder Bros. Co.* (C.A. 5, 1966), 367 F. 2d 980, 984; P.L. 773, June 25, 1948, 1948-2 C.B. 321; Internal Revenue Code of 1954, sec. 7482.

In the process of adopting that amendment the Dobson rule was severely and lengthily criticized on the floor of Congress. Title 28, United States Code, Congressional Service, 80th Cong., 2d Sess., p. 1986, *et seq.,* especially 1990-1991, 2000, 2005, 2010-2011, 2037-

[1]This refers to the appendix in the petition.

2039. The rule, it was charged, had resulted in "confusion." That was also the effect attributed to it by the dissents in *Kelley, supra.* Justice Rutlege there, at page 533, pointed out especially the destructive effect of the Dobson rule in allowing, on the basis of differences without substance, "squarely conflicting" decisions. In the debates in Congress cited above it was observed, page 1990, that this Court, in *Trust of Bingham v. Commissioner,* 325 U.S. 365, had sought to cure *Dobson* but that in *Kelley, supra,* it had "wiped out its [*Bingham's*] curative effectiveness, and left the Dobson doctrine again supreme." It was no wonder that after *Kelley* Congress so quickly put an end to the Dobson rule.

Respondent here, under his point 2, is obviously misled by the *Kelley* case. The Court of Claims in *Morse* and *Ginsburg*[2] did point out some differences between the case here and the cases there. But only a difference between them as to the time when the change of purpose shown occurred could be a difference of any substance and, as shown in our petition, pages 8-9, the Court of Claims, in *Morse* and *Ginsburg* placed the change of purpose definitely at August 10, 1956, and as shown in our petition, at page 13, and in this reply under point 1 above, the record here is clearly consistent with that date. As far as substance is concerned, therefore, the failure here to recognize the change of purpose by that date is a clear and direct conflict between the case here and the cases there.

Nor is that conflict merely one of fact. As shown at pages 10-11 of the petition herein, the court below in arriving at its conclusion in respect to the purpose of

[2]371 F. 2d 474 and 396 F. 2d 983, respectively.

SBIC in holding the property clearly erred on the quantum of petitioners' burden of proof. Further, because of petitioners' burden of proof it stated that it could not "hold as a matter of law that that purpose [of holding the property] *must* have changed." (Pet. App. 26; italics in original.) As shown in the final paragraph under point 3 below, this in itself was error. Thus we have a conflict of fact induced by a compound of errors of law. The conflict between the court below herein and the Court of Claims in *Morse* and *Ginsburg* is thus clearly not merely one of fact, as respondent here, at page 5, suggests.

3. Under his point 3, at page 6, respondent in effect concedes a clear conflict with decisions of this Court by implying that petitioners must demonstrate, "conclusively," the absence after Berger's sale of a purpose to hold primarily for sale to customers in the ordinary course of trade or business. Petitioners' burden of proof, even if it were not of a negative but of a positive, would never be required to be *conclusive. Burnett v. Niagara Falls Brewing Co.,* 282 U.S. 648, 654, cited by petitioners in their petition, at page 11; *United States v. United States Gypsum Co.,* 333 U.S. 364, 395. Nor is petitioners' burden one to show, as respondent finally suggests, that the evidence "cannot support" the findings actually made; for "when although there is *evidence to support it* [a finding], the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed," reversal is proper. (Italics supplied.)

United States v. United States Gypsum Co., supra, at pages 395-396.

The cases cited by respondent in that connection, *United States v. National Association of Real Estate Boards,* 339 U.S. 485, 495-496, and *United States v. Yellow Cab Co.,* 338 U.S. 338, 342, are not to the contrary. Indeed, the later of those two cases, *United States v. National Association of Real Estate Boards,* at the pages indicated, being the very pages cited by respondent, cites and relies on *United States v. United States Gypsum Co., supra.*

Just as respondent thus ran counter to decisions of this Court in saying that petitioners failed to prove the required absence of holding for sale to customers "conclusively," and in saying that petitioners failed to show that the evidence "cannot support" the finding to the contrary, so likewise did the court below in saying that it could not "hold as a matter of law that that purpose [of holding the property] *must* have changed." (Pet. App. 26; italics in original.)

4. It is very significant also that respondent has wholly failed to respond to points 3, 4 and 5 of the petition. (Pet. 12-15.) The conflicts shown there between the decision below and decisions of this Court are critical in the law of taxation and reach into the general principles of justice. We urge a restudy of those points.

5. The inconsistency between the decision here below and the result in *Morse* and *Ginsburg* in the

Court of Claims, referred to in point 2 of this reply, is emphasized by respondent's failure also to respond to point 6 of the petition. (Pet. 6-7, 16.) As there shown, the case here was reopened by the Internal Revenue Service "in the interest of being consistent" with the cases which finally were decided in the Court of Claims. As there also shown, the consistency which was thus a matter of such importance to the Internal Revenue Service is lost as a result of the reverse conflict represented by the present posture of the same cases.

The importance of consistency to the Internal Revenue Service is further shown by its present rule on reopening of cases. According to that rule the Internal Revenue Service will not reopen any case to make an adjustment unfavorable to the taxpayer, because of an error involved in the prior closing, unless that error was "a clearly defined substantial error based on an *established* Service position existing at the time of the previous examination." Revenue Procedure 68-28, 1968-33 I.R.B. 41, Sec. 4.01(2). (Italics supplied.) Thus to warrant reopening of a case, as occurred here, error in the prior closing is not enough; the reopening must, in effect, be required by consistency. Consistency is, of course, an element of basic justice, but here, more especially, it is a requirement of Internal Revenue policy. For that reason we raise again the importance of this case.

SUPPLEMENTAL BRIEF.

A further conflict has just resulted because of the decision August 22, 1968, by the United States Court of Appeals for the Tenth Circuit in *Commissioner v. Tri-S Corporation,* 68-2 USTC ¶9541. There the Commissioner appealed from a decision of the Tax Court, 48 T.C. 316, and the Court of Appeals affirmed.

The taxpayer there was a residential land developer. Involved in the case was a particular 20-acre tract. Because of notice by the State of Colorado on April 7, 1961, that it would institute condemnation proceedings to take the tract for highway purposes, the taxpayer entered into negotiations with the State for sale of the tract to it. Agreement was reached on July 25, 1961, and conveyance to the State was completed on October 6, 1961. The Court there stated:

> "During the period from April 7, 1961, to October 6, 1961, it is clear under the facts that the taxpayer was not holding the 20-acre tract primarily for sale to customers in the ordinary course of its trade or business. While prior to April 7, 1961, it had intended at some time in the future to improve the 20-acre tract, so as to render it suitable for a shopping center and to make disposition of it for that purpose, from and after that date it would have been futile for it to have undertaken to carry out such future plans. It clearly did not hold such land for sale to customers in the ordinary course of its trade or business on July 25, 1961, when it agreed to convey the 20-acre tract to the State of Colorado, and on October 6, 1961, when it consummated such conveyance."

In the case here, in addition to other factors supporting petitioners, it is wholly uncontested that after August 10, 1956, and up to the time of the sales involved of petitioners' interests in SBIC, SBIC was just holding the land and was not, either directly or indirectly, developing it, or making any plans to develop it, or offering it for sale, in its raw state or any other state, to customers in the ordinary course of its trade or business. There is absolutely nothing in the findings to the contrary. The conflict with the *Tri-S* case is thus clear and direct.[3]

Conclusion.

Because of the conflicts recited herein, and in our petition, between the decision below and decisions of this and other courts, and because of the importance of this case shown above, we urge again that our petition for a writ of certiorari be granted.

Respectfully submitted,

GEORGE T. ALTMAN,
Attorney for Estate of Eugene L. Freeland, deceased, and Vera Good Freeland.

ADAM Y. BENNION,
Attorney for Margaret C. Lowthian.

Both by GEORGE T. ALTMAN,
Attorney.

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[3]In view of the fact that this supplemental brief presents a conflict with a case which had not yet been decided when the petition herein was filed, petitioners recognize that respondent should have an opportunity to file a response.

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IN THE

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OCTOBER TERM, 1968
No. 341

ESTATE OF EUGENE L. FREELAND, Deceased, by SECURITY FIRST NATIONAL BANK, a national banking association, Executor, and VERA GOOD FREELAND, by L. N. TURRENTINE, Conservator,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

MARGARET C. LOWTHIAN,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Motion to Delay Action on Petition for Rehearing.

GEORGE T. ALTMAN,
424 South Beverly Drive,
Beverly Hills, Calif. 90212,

ADAM Y. BENNION,
523 West Sixth Street,
Los Angeles, Calif. 90014,
Attorneys for Petitioners.

Parker & Son, Inc., Law Printers, Los Angeles. Phone MA. 6-9171.



IN THE

Supreme Court of the United States

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Motion to Delay Action on Petition for Rehearing.

As to the case of *Commissioner of Internal Revenue v. Tri-S Corporation,* C.A. 10, 68-2 USTC ¶9541, referred to in the petition for rehearing herein filed concurrently herewith, it would appear that respondent has until November 20, 1968, in which to petition this Court for a writ of certiorari in that case.

We believe very strongly that if respondent does file such petition in the *Tri-S* case and this Court determines to review that case, it will have no additional burden in reviewing the case here. On the contrary, we believe that a review of this case will be greatly helpful to the Court in a review by it of the *Tri-S* case.

For that reason we respectfully move the Court at least not to take action on the petition for rehearing herein until after the time for a petition for certiorari in the *Tri-S* case has expired, and if such a petition is filed, until a decision on that petition is made.

This motion is not intended as a limitation on the petition for rehearing herein.

Respectfully submitted,

GEORGE T. ALTMAN,
Attorney.

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PETITION FOR REHEARING.

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Respondent.

PETITION FOR REHEARING.

Petitioners now petition this Court for a rehearing of their petition for a writ of certiorari.

The reason for this petition is that when the petition for certiorari was denied this Court may not yet have had an opportunity to consider the supplemental brief filed by petitioners under a single cover with their reply. That supplemental brief sought to bring to this Court's attention what petitioners believed, and still believe, to be a direct conflict between the opinion herein below and the case of *Commissioner of Internal Revenue v. Tri-S Corporation,* decided by the United States Court of Appeals for the Tenth Circuit August 22, 1968, and reported at 68-2 USTC ¶9541.

Petitioners therefore urge a reconsideration of their petition for writ of certiorari and especially a study, or restudy, for that purpose of the said supplemental brief.

Respectfully submitted,

GEORGE T. ALTMAN,
Attorney.

Certificate of Counsel.

Undersigned counsel hereby certifies that the above petition is presented, not for delay, but in good faith and in the well considered belief that it is justified by the reasons stated; and further that it is restricted to the grounds stated in Rule 58(2) of this Court.

GEORGE T. ALTMAN